

Message Text

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ACTION ARA-14

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L-03 NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15
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E.O. 11652: N/A
TAGS: EGEN, EFIN, ETRD, EALR, VE
SUBJECT: GOV MOVES TO CONTROL INFLATION

1. SUMMARY: PRESIDENT PEREZ ANNOUNCED JULY 10 NUMBER OF MEASURES DESIGNED TO REDUCE INFLATIONARY PRESSURE THROUGH PRICE CONTROLS, CREDIT RESTRAINTS, GOVERNMENT SPENDING REDUCTIONS AND INCREASED RESERVE REQUIREMENTS FOR BANKING INSTITUTIONS. INTENT OF NEW MEASURES, WHICH TAKE EFFECT IMMEDIATELY, IS TO REDUCE THE RATE OF GROWTH OF THE MONEY SUPPLY, THUS REDUCING DEMAND FOR GOODS AND SERVICES IN THE OVERHEATED ECONOMY. LOCAL INTEREST GROUPS HAVE NOT YET HAD SUFFICIENT TIME TO ASSESS NEW MEASURES, ALTHOUGH WE WOULD EXPECT REACTION TO BE GENERALLY FAVOURABLE WITH EXCEPTIONS OF HOUSING AND CONSTRUCTIONS SECTORS, WHICH HAVE HAD SPECIAL CONSTRAINTS IMPOSED. WE EXPECT THE MEASURES TO BE ONLY PARTIALLY SUCCESSFUL IN ACHIEVING INTENDED GOAL. CREDIT CONSTRAINTS SHOULD BE HELPFUL, BUT PRICE CONTROLS, ESPECIALLY IN HOUSING, WILL ONLY EXACERBATE CURRENT SHORTAGES WITHOUT LASTING BENEFIT TO VENEZUELAN ECONOMY. MAJOR ELEMENT STILL LACKING FOR COMPREHENSIVE ANTI-INFLATION PROGRAM IS MEANINGFUL TAX REFORM. END SUMMARY.

2. IN A SPEECH DELIVERED BEFORE THE ANNUAL ASSEMBLY OF FEDECAMARAS (NATIONAL ASSOCIATION OF CHAMBER OF COMMERCE)
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JULY 10, VENEZUELAN PRESIDENT PEREZ ANNOUNCED A SERIES OF MEASURES WHICH HE DESCRIBED AS BRAKES ON THE GROWTH OF INFLATION, SPECULATION AND CONSUMERISM IN VENEZUELA. MAJOR MEASURES ANNOUNCED BY THE PRESIDENT INCLUDE THE FOLLOWING:

-PURCHASES MADE WITH CREDIT CARDS MAY NOT BE FINANCED
FOR A PERIOD OF LONGER THAN ONE MONTH. ENTIRE BALANCE

DUE MUST BE PAID WITHIN THIRTY DAYS.

-RESERVE REQUIREMENTS ON OFFICIAL DEPOSITS ARE RAISED
TO 75 PERCENT.

-A 50 PERCENT RESERVE REQUIREMENT ON DEPOSITS IN VENEZUELAN
BANKS BY NON-RESIDENTS OF VENEZUELA.

-AUTOMOBILE PURCHASES MAY NOT BE FINANCED FOR A PERIOD
OF LONGER THAN 24 MONTHS FOR PRICE REGULATED MODELS AND
18 MONTHS FOR ALL OTHER MODELS.

-100PERCENT OF THE FUNDS WHICH FINANCIAL INSTITUTIONS ARE REQUIRED
TO USE TO FINANCE REAL ESTATE TRANSACTIONS MUST BE USED
TO FINANCE THE PURCHASE OF HOUSING. ONLY AMOUNTS IN EXCESS
OF THE MINIMUM REQUIREMENT MAY BE USED FOR OTHER TYPES OF
REAL ESTATE TRANSACTIONS.

-RENTS MAY NOT BE INCREASED BY MORE THAN 15 PCT ANNUALLY.

-THE SALES PRICE FOR REAL ESTATE MAY NOT EXCEED 130PCT
OF THE VALUATION PLACED ON THE PROPERTY BY THE FINANCING
INSTITUTION.

-PRICES ARE FROZEN AT THEIR JULY 1 LEVEL FOR CLOTHING,
FOOTWEAR, COSMETICS, SERVICES RENDERED BY BARBERS AND
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HAIRDRESSERS, AND RESTAURANT PRICES.

-1978 GOV CURRENT BUDGETARY EXPENDITURES MAY NOT
EXCEED THE 1977 LEVEL.

- MINISTRIES AND OTHER GOVERNMENT AGENCIES MAY NOT FILL
VACANCIES EXISTING ON JUNE 30, 1977.

-MINISTRIES AND OTHER AGENCIES MAY NOT BUY OR RENT
ADDITIONAL OFFICES FOR AN IDEFINITE PERIOD.

3. BUSINESS, LABOR AND OTHER SPECIAL INTERESTS IN VENEZUELA HAVE
NOT HAD SUFFICIENT TIME TO REACT DEFINITELY TO THE NEW PROPOSALS.
WE WOULD EXPECT, HOWEVER, THAT THE REACTION WILL BE A MIXED ONE,
WITH ALMOST UNIVERSAL PRIVATE SECTOR APPROBATION FOR THE
MEASURES INTENDED TO CONTROL GOVERNMENT SPENDING, AND LESS
ACCEPTANCE FOR MEASURES DESIGNED TO CONTROL SPECULATION AND
PROFITEERING. LABOR INTERESTS WILL CERTAINLY APPLAUD THE
GOVERNMENT'S EFFORTS TO CONTROL INCREASES IN THE COST OF HOUSING,
CLOTHING AND OTHER GOODS AND SERVICES.

4. MOST INFORMED OBSERVERS, INCLUDING GOVERNMENT OFFICIALS,

HAVE BECOME INCREASINGLY CONCERNED ABOUT THE RAPID GROWTH IN IMPORTS, THE MONEY SUPPLY AND THE LEVEL OF GOVERNMENT EXPENDITURES. DURING THE PAST FOUR YEARS VENEZUELAN MONETARY AND CREDIT POLICIES HAVE BEEN DESIGNED TO CONTROL PRICE INCREASES BUT HAVE MET WITH ONLY LIMITED SUCCESS. THE FUNDAMENTAL MEASURE IN THE FIELD OF MONETARY POLICY, WAS, OF COURSE, THE DECISION TO ALLOCATE OVER \$5 BILLION TO THE VENEZUELAN INVESTMENT FUND. THIS ACTION PREVENTED THE MONETIZATION OF HUGE SUMS OF FOREIGN EXCHANGE. IN ADDITION, THERE WERE A SERIES OF MEASURES INTRODUCED IN APRIL OF 1976 WHICH WERE INTENDED TO DAMPEN INFLATIONARY PRESSURES BY REDUCING LIQUIDITY IN THE BANKING SYSTEM. HOWEVER, THESE MEASURES HAVE BEEN ONLY PARTIALLY SUCCESSFUL (THE CPI ROSE BY 7.5PCT DURING THE APRIL 1976-77. PERIOD, A MAJOR INCREASE BY VENEZUELAN STANDARDS) IN LIMITED OFFICIAL USE

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PART BECAUSE OF INFLATIONARY PRESSURES PRODUCED BY GRANDIOUS DEVELOPMENT SCHEMES AND INCREASED GOVERNMENT SPENDING. IN FACT, DESPITE SOME RATHER SOUND DECISIONS BY THE GOV, THE MONEY SUPPLY GREW BY 47PCT IN 1975 AND 24PCT IN 1976, WHILE REAL GDP GROWTH DID NOT EXCEED 6PCT IN EITHER YEAR.

5. WE WOULD EXPECT THE NEW MEASURES TO BE ONLY PARTIALLY SUCCESSFUL IN ACHIEVING THEIR INTENDED PURPOSE. LIMITATIONS ON CONSUMER CREDIT SHOULD DAMPEN DEMAND FOR A WIDE RANGE OF GOODS, MANY OF WHICH ARE IMPORTED. THE PROPOSED CEILING ON THE LEVEL OF CURRENT GOVERNMENT EXPENDITURES, IF SUCCESSFULLY IMPLEMENTED (AND WE HAVE DOUBTS ABOUT THIS), SHOULD REDUCE THE PROBABILITY OF DEFICIT BUDGETS OCCURRING DURING THE NEXT TWO OR THREE YEARS, THUS REDUCING INFLATIONARY PRESSURES. BUT THOSE PROPOSALS WHICH CALL FOR PRICE CONTROLS ON REAL ESTATE AND SELECTED GOODS AND SERVICES ARE NOT LIKELY TO BE ANY MORE EFFECTIVE THAN SIMILAR MEASURES IN THE PAST. FOR EXAMPLE, PRICE CONTROLS ON ESSENTIAL FOOD ITEMS HAVE PRODUCED WIDESPREAD SHORTAGES OF COMMODITIES SUCH AS MEAT, POTATONS, MILK, EGGS, ETC. EVENTUALLY, THE GOV HAD TO BOW TO PRESSURES AND PERMIT PRICE INCREASES. RENT CONTROLS AND LIMITS ON PROFITS FROM THE SALE OF REAL ESTATE ARE LIKELY TO EXACERBATE THE CURRENT HOUSING SHORTAGE IN VENEZUELA WITHOUT ACHIEVING ANY LASTING BENEFIT FOR THE CONSUMER. BUT NATIONAL ELECTIONS ARE SCHEDULED TO TAKE PLACE IN DECEMBER OF 1978, AND UNOFFICIAL ELECTIONEERING HAS ALREADY BEGUN. INFLATION AND THE LEVEL OF GOVERNMENT EXPENDITURES HAVE ALREADY BECOME CAMPAIGN ISSUES AND THE GOVERNMENT WANTS TO SEEM TO BE DOING SOMETHING ABOUT THESE PROBLEMS. MEANINGFUL TAX REFORM, THE ONE MEASURE THE GOV COULD IMPLEMENT WHICH WOULD AT ONCE REDUCE CONSUMER DEMAND, REDUCE THE LIKELIHOOD OF FUTURE GOVERNMENT BUDGETARY DEFICITS AND REDUCE THE GROWING PRESSURE ON THE BALANCE OF PAYMENTS, IS SIMPLY NOT IN THE CARDS. THE CURRENT SERIES OF TAX PROPOSALS

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PENDING BEFORE CONGRESS WILL ACHIEVE NONE OF THESE GOALS, IN
THE ABSENCE OF BASIC FISCAL REFORM, GOVERNMENT EFFORTS ON
THE MONETARY SIDE CAN ONLY MEET WITH PARTIAL SUCCESS AT BEST.
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